

Appeal of Louis and Ann Dulien

Appellants are residents of the State of Washington and filed nonresident California returns during the appeal years. The amount of California income reported on those returns is as follows:

<u>Year</u>	<u>Amount</u>	<u>Source</u>
1968	\$17,336.00	Unnamed California warehouse-rent
	23,480.00	United Engineering Co., a partnership, San Francisco
1969	\$24,801.53	United Engineering Co.
1970	\$32,960.28	Unnamed partnership
1971	\$40,284.37	Unnamed partnership

On their returns, appellants claimed deductions for interest payments and legal expenses allegedly connected with California business interests. Following an audit, respondent disallowed these deductions for lack of substantiation. At the protest level, appellants presented an amended schedule of business expenses which included an additional deduction for payment of California real and personal property taxes. The record shows that respondent requested several times that appellants' representative provide supporting information concerning all of the aforementioned deductions, but the response was incomplete. Following the protest hearing, respondent affirmed its proposed assessments and this appeal followed.

The sole issue to be decided is whether appellants adequately substantiated their claimed business deductions for payments of interest, legal fees and real property taxes.

It is well established that the taxpayer has the burden of proving his entitlement to claimed deductions. (New Colonial Ice Co. v. Helvering, 292 U.S. 435 [78 L. Ed. 1348] (1934); Appeal of James? Denny, Cal. St. Bd. of Equal., May 17, 1962.) Thus, in order to deduct expenses incurred in carrying on a business (Rev. & Tax. Code, § 172021, appellants must produce detailed records of the expenditures, including their business nature. (Appeal of National Envelope Corp., Cal. St. Bd. of Equal., Nov. 7, 1961.) In addition, as nonresidents, appellants must establish a connection between the claimed deductions and income arising from a California source. (Rev. & Tax. Code, § 17301.)

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Interest on Loans

Appellants borrowed money from California banks and advanced the money to two California corporations owned by appellants' children. The corporations were apparently unable to pay appellants the interest on these loans so appellants paid it and claimed deductions for the payments, which respondent disallowed.

We believe respondent's action must be upheld. The record does not establish that the interest was paid on loans made in connection with a California business belonging to appellant. All that is shown is that a personal loan was made to appellants who in turn made a personal loan motivated by a family relationship. Under no circumstances may a nonresident taxpayer deduct interest paid on personal loans. (Cal. Admin. Code, tit. 18, req. 17301-17302, subd. (5).) Absent any significant evidence in support of the claimed deduction, the disallowance must be affirmed. (Appeal of Myron E. and Alice Z. Gire, Cal. St. Bd. of Equal., Sept. 10, 1969.)

Legal Fees

Appellants claimed deductions for legal fees for services rendered in 1969 and 1970 in connection with the condemnation sale of appellants' property in Los Angeles. No information was provided describing the nature of the legal services, the property itself or its relationship to any income producing activity in California, despite several requests by respondent. Other legal fees allegedly incurred in the years 1969 through 1971 are not described at all. Appellants' failure to come forth with any evidence to support their general allegations of expenses incurred justified respondent's disallowance of the deductions and we affirm that action. (Appeal of Robert V. Erilane, Cal. St. Bd. of Equal., Nov. 12, 1974.)

Property Taxes

In 1967 appellant Louis Dulien relinquished to his children ownership of the corporate stock of Steel Products Supply, Inc., while apparently retaining title to the land on which the corporate business was situated. Appellants submitted copies of property tax bills showing Louis Dulien as owner of record, along with copies of cancelled checks, as evidence of payment of the taxes on the described land. Appellants also presented evidence of payment of a tax bill covering the business personal property of Steel Products Supply, Inc. Payments to the

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Los Angeles County Tax Collector were shown in the following amounts: (1) \$9,116.36 paid by Louis Dulien on April 6, 1970; (2) \$9,935.46 paid by Steel Products Supply, Inc., on December 9, 1970, reimbursed by Louis Dulien on December 11, 1970; (3) \$10,579.18 paid from Louis Dulien account on December 9, 1971; and (4) \$4,913.11 paid by Louis Dulien on August 24, 1971. Respondent disallowed the real and personal property tax deductions for lack of substantiation.

However, we believe the record here justifies, allowance of the real property tax deductions under the authority of section 17204 of the Revenue and Taxation Code, which allows a deduction for payment of local real property taxes. Appellants, as nonresidents, may claim such a deduction even though the taxes paid are not connected with income from sources within California. (Rev. & Tax. Code, § 17302.) Generally, this deduction is available only to the person on whom the taxes are imposed. (Cal. Admin. Code, tit. 18, req. 17204(a).) In this case Louis Dulien, as the owner of record of the property located at 11611 South Alameda Street, Los Angeles, was primarily liable for the taxes on that property, and may claim deductions for paying them. Even though the December 9, 1970, payment was made by Steel Products Supply, Inc., the payment was Louis Dulien's personal liability, was paid by him through Steel Products Supply, Inc., and is therefore deductible by him. (See Edward C. Kohlsaat, 40 B.T.A. 528 (1939).)

A contrary result is reached concerning appellants' payment in 1971 of personal property taxes in the amount of \$4,913.11. This amount was assessed against Steel Products Supply, Inc., and in order for taxes to be deducted as such, they must be paid by the one on whom they were imposed. (John Patrick Feeney, 1166,009 P-H Memo. T.C. (1966).) Accordingly, we uphold respondent's disallowance of a deduction for payment of personal property taxes but must reverse respondent's disallowance of deductions for real property taxes paid.

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O R D E R

Pursuant to the views expressed in the opinion of the board on file in this proceeding, and good cause appearing therefor,

IT IS HEREBY ORDERED, ADJUDGED AND DECREED, pursuant to section 18595 of the Revenue and Taxation Code, that the action of the Franchise Tax Board on the protest of Louis and Ann Dulien against proposed assessments of additional personal income tax in the amounts of \$2,574.70, \$839.90, \$1,746.66 and \$1,306.39 for the years 1968, 1969, 1970 and 1971, respectively, be and the same is hereby modified in that deductions for real property taxes paid are to be allowed in accordance with the opinion on file herein. In all other respects, respondent's action is sustained.

Done at Sacramento, California, this 26th day
of July , 1978, by the State Board of Equalization.

George R. Huey, Chairman
Philip K. O'Brien, Member
William B. Bunker, Member
Iris Sankey, Member
_____, Member